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IN THE

Supreme Court of the United States

OCTOBER TERM, 1981

F. W. WOOLWORTH CO., *Appellant,*

v.

TAXATION AND REVENUE DEPARTMENT OF THE STATE OF NEW MEXICO, *Appellee.*

Appeal from the Supreme Court of New Mexico

REPLY BRIEF OF APPELLANT

GEORGE W. BEATTY
(Counsel of Record)
WILLIAM L. GOLDMAN
JAMES A. RIEDY
1200 18th Street, N.W.
Washington, D.C. 20036
(202) 457-8528

MICHAEL D. BRAY
30 Rockefeller Plaza
New York, N.Y. 10112

Counsel for Appellant

ARNOLD S. ANDERSON
ALAN J. LIPNER
233 Broadway
New York, N.Y. 10279

Of Counsel

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REPLY BRIEF OF APPELLANT[1]

This brief responds to certain arguments advanced by the Taxation and Revenue Department of the State of New Mexico ("New Mexico") in its brief and by the Multistate Tax Commission ("MTC") in its *amicus* brief.

I. THE INCLUSION OF THE DIVIDENDS, EXCHANGE GAIN, AND GROSS-UP IN APPORTIONABLE BUSINESS INCOME CONTRAVENES THE DUE PROCESS CLAUSE.

It is now clear from New Mexico's brief that the State seeks a result that is in conflict with this Court's holding in *Mobil Oil Corp.* v. *Commissioner of Taxes of Vermont,* 445 U.S. 425 (1980) (hereinafter

[1] As required by Rule 28.1 of the Rules of this Court, a list of appellant's subsidiaries (other than wholly owned subsidiaries) and affiliates is set forth on page (i) of the Brief of Appellant.

"Mobil"). In *Mobil*, this Court upheld the inclusion of dividends in apportionable business income only after first determining that Mobil's business activities and those of the payor corporations were sufficiently integrated so as to constitute parts of the same unitary business. Thus, as this Court noted (445 U.S. at 441), had Mobil—

> . . . chosen to operate its foreign subsidiaries as separate divisions of a legally as well as a functionally integrated enterprise, there is little doubt that the income derived from those divisions would meet due process requirements for apportionability. Cf. *General Motors Corp.* v. *Washington*, 377 U.S. 436, 441 (1964). Transforming the same income into dividends from legally separate entities works no change in the underlying economic realities of a unitary business, and accordingly it ought not to affect the apportionability of income the parent receives. [Footnote deleted.]

New Mexico expressly acknowledges that *Mobil* involved a situation where a single unitary business was conducted in a multicorporate form (*i.e.*, by both the recipient and the dividend-paying corporations) so that the dividends were paid out of the earnings of the unitary business. (N.M. Br. 22-23) New Mexico also acknowledges that this is not the case here, stating (N.M. Br. 15):

> The parties have no disagreement as to the boundaries of Woolworth's unitary business. Both the taxpayer and New Mexico describe Woolworth as operating a unitary business in the fifty states, Puerto Rico and the Virgin Islands.

This statement constitutes clear recognition by New Mexico that appellant did not conduct a unitary retail

business with any of its foreign, dividend-paying subsidiaries. New Mexico has even stated in so many words that it would not have included the income of those subsidiaries in apportionable business income if their operations had been conducted directly by appellant in divisions. (N.M. Br. 29, n.32)

Thus, New Mexico has finally recognized that the record in this case (see appellant's brief, pp. 19-25) compels the conclusion that appellant was *not* conducting a single, unitary business with its foreign subsidiaries.[2] By so agreeing, New Mexico has effectively repudiated the grounds on which the New Mexico Supreme Court based its decision. That court upheld the apportionability of the dividends in issue only after first concluding, as it was requested to do by New Mexico, that the "functional integration" test of *Mobil* was satisfied.[3] In this regard, the New Mexico Supreme Court stated (J.S. App. A 19a):

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[2] New Mexico's concession based on the record in this case involving the fiscal year 1977 is in no way diminished by a recent California Superior Court Memorandum concluding that appellant and its Canadian subsidiary were engaged in a unitary business during the period 1961-1964. See *F. W. Woolworth Co.* v. *Franchise Tax Board of the State of California* (Cal. Sup. Ct. Dept. No. 19, Docket No. 656 793), Notice of Intended Decision dated Feb. 3, 1982.

[3] New Mexico filed a supplemental brief in the New Mexico Supreme Court, following this Court's decision in *Mobil*, in which New Mexico stated (p. 3):

> Throughout this appeal, the Department has argued that it is not necessary for the taxpayer and its foreign subsidiaries to be a unitary business, in order to call the dividend income 'business income.' The Supreme Court, however, seems to find it necessary that the businesses be unitary, if the income from one to the other is to be apportioned by a state. That portion of the *Mobil* opinion has little impact on this case, because the Hearing Officer found Woolworth to be unitary with its foreign subsidiaries and Woolworth has not shown otherwise.

> On the due process issue and in conformity with *Mobil,* we hold that, for income tax considerations, there is substantial evidence in this record that Woolworth was conducting a unitary business with its foreign subsidiaries and that there is a sufficient nexus between the corporation and the State of New Mexico to justify an apportioned tax on these dividends. The income is obviously related to the mutual activities of the parent and its affiliates. The control over the subsidiaries, the interdependence, the history of the relationships, the placing of the money in the general operating account, all point to functional integration and reveal an underlying unitary business for our purposes here.

By now conceding that appellant did *not* conduct a unitary business with its foreign subsidiaries, New Mexico has effectively conceded its case.

New Mexico is now left with an untenable position that unavoidably contradicts this Court's reasoning in *Mobil.* Although the whole teaching of Mobil is that the taxpayer's corporate structure (445 U.S. at 441) "ought not to affect the apportionability of income the parent receives," New Mexico seeks just the opposite result here. In *Mobil,* this Court held that apportionability should not change simply because the taxpayer chooses to conduct certain business activities in separate subsidiaries. By contrast, New Mexico seeks to include the dividends in issue in apportionable income *solely* because appellant has chosen to conduct certain foreign activities in separate subsidiaries. New Mexico's entire case turns on differences in corporate structure and the perception of the income in issue as "income from intangibles"—as contrasted with operating

income.[4] Such an approach cannot be reconciled with this Court's approach in *Mobil*.

Quite surprisingly, New Mexico cites *Mobil* for the proposition that dividends should be treated like other income. (N.M. Br. 23) We agree. It is New Mexico which applies the double standard. This is fully demonstrated by New Mexico's reasons (N.M. Br. 16-17) for treating the dividends as apportionable business income. For example, New Mexico relies on the large number of Woolworth stores worldwide, consolidated financial statements, placing dividends in the general treasury, and other similar factors. Those factors were dealt with in appellant's brief (pp. 19-25) as part of our demonstration that appellant did not conduct a unitary business with its foreign subsidiaries. Given that showing (with which New Mexico agrees), why should those factors be sufficient to justify the apportionment of dividends when (as New Mexico admits) those factors would not be sufficient to justify apportionment if the foreign subsidiaries were operated as divisions of Woolworth? Why should those factors be any more pertinent to the business relationship between appellant's domestic Unitary Business and the ownership of stock in foreign subsidiaries than those factors would be to the business relationship between appellant's domestic Unitary Business and the

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[4] New Mexico has stated (N.M. Br. 29) that it would not tax the income of the foreign retail operations if those operations were conducted directly as divisions of appellant. Yet New Mexico seeks to tax dividends paid out of that income as a consequence of conducting the foreign retail operations in subsidiaries. The only difference between the two situations involves appellant's choice of corporate structure.

direct conduct of foreign operations in divisions? Why should a State be allowed to expand its taxing authority solely because stock ownership is involved?

Appellant, on the other hand, seeks to apply *Mobil* consistently by treating dividends like other income. Under *Mobil*, 445 U.S. at 439, the "linchpin of apportionability in the field of state income taxation is the unitary-business principle." In the case of dividends from substantial operating subsidiaries, this means that apportionability is permissible only where the activities of the recipient and payor corporations are parts of a single, functionally integrated business.

Nonetheless, New Mexico asserts (N.M. Br. 23) that dividends are apportionable as business income so long as "the taxpayer's investment in the dividend paying corporations contributes to and enhances the value of the taxpayer's business" even though "such corporations are not a unitary part of the taxpayer's business." Similarly, the MTC asserts that dividends may be apportioned as long as the stock investment is "rationally related" to the taxpayer's unitary business. (MTC Br. 8-9, 16-17) These tests are too broad. They are also inconsistent with the rationale for apportionability (see pages 14-17 of our main brief) and unsupported by the cases cited by New Mexico (N.M. Br. 16-19).[5]

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[5] For example, in *W. R. Grace & Co.* v. *Commissioner of Rev.*, 378 Mass. 577, 393 N.E.2d 330 (1979), involving the gain from Grace's sale of its stock in the Miller Brewing Company, the court noted (393 N.E.2d at 335): "[t]he record and the findings of the board indicate the Miller holding was acquired by Grace in order to bolster and expand its unitary operations." Grace also acknowledged (*ibid.*) "that all its operating businesses in the United States, including its Massachusetts activities, are unitary for the purposes

In our main brief, we noted (pp. 18-19) that there may be situations not discussed in *Mobil*, and not present here, in which a stock investment is sufficiently related to a taxpayer's unitary business to justify apportionment of the dividends even though the taxpayer is not conducting a unitary business with the dividend-paying corporation. We referred, for example, to dividends received by a securities dealer on stocks held in inventory for sale to customers. Another example would be income from short-term investments of working capital used in the unitary business. See, *e.g.*, *Sperry & Hutchinson Co.* v. *Dept. of Rev.*, 270 Ore. 329, 527 P.2d 729 (1974). However, these exceptions to the "functional integration" test of *Mobil* have no applicability in cases such as this or *Mobil*, involving investments in large, operating subsidiaries. New Mexico's case essentially amounts to nothing more than an

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of State taxation." Under these circumstances it is reasonable to infer that Massachusetts would have treated Grace's portion of the Miller operations as part of Grace's unitary business if Miller had been liquidated and operated as a joint venture. Similarly, in the other cases cited by New Mexico involving other types of income from intangibles, the courts have been careful to analyze the functional relationship between the intangibles involved and the unitary business. In *Sperry & Hutchinson Co.* v. *Dept. of Rev.*, 270 Ore. 329, 527 P.2d 729 (1974), for example, the court held that certain short-term securities were held in connection with the taxpayer's business and that other short-term securities and long-term securities were not held in connection with the taxpayer's business. See also *Qualls* v. *Montgomery Ward & Co., Inc.*, 266 Ark. 207, 585 S.W.2d 18 (1979); *Xerox Corp.* v. *Comptroller of Treasury*, 290 Md. 126, 428 A.2d 1208 (1981). Appellant does not necessarily concede the correctness of these decisions. But they cannot properly be cited, as New Mexico seeks to do, as support for a more relaxed unitary business test where business operations are conducted in separately incorporated subsidiaries.

assertion that dividends from large subsidiaries are always apportionable because it is advantageous or profitable to own large subsidiaries. Such a broad proposition cannot be reconciled with this Court's opinion in *Mobil*.[6] Thus, even if this Court should hold that functional integration is not necessary in every case, more must be required than is present here for dividends to be includible in apportionable income.

This does not mean, as New Mexico asserts, that we have disregarded the distinction between a parent corporation and its subsidiary. For example, New Mexico states (N.M. Br. 11) that "[t]he substance of Woolworth's contention is that dividend income may be taxed by a state only if that state has jurisdiction to tax the payor of the dividends." That is not so. We recognize that the dividends in issue are part of appellant's income which may, for due process purposes, be taxed by the State of commercial or legal domicile. However, as this Court explained in *Mobil* (445 U.S. at 439), it is necessary to evaluate the relationship between appellant's foreign subsidiaries and its domestic Unitary Business in order to determine whether the dividend income is part of the apportionable income of that Business (and therefore also subject to tax in every State in which the Business is conducted) or is income of a "discrete business enterprise" (and therefore not subject to apportionment). See also *Mobil*, 445 U.S. at 445-446. And for this purpose, it is essential, as was done in *Mobil*, to examine the relationship between appellant's domestic Unitary

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[6] "We do not mean to suggest that all dividend income received by corporations operating in interstate commerce is necessarily taxable in each State where the corporation does business." *Mobil*, 445 U.S. at 441-442.

Business and the underlying activities of the payor corporations. In this case, appellant's domestic Unitary Business and the operations of its foreign subsidiaries are "discrete business enterprises."

II. ALTERNATIVELY, THE DUE PROCESS CLAUSE AND THE COMMERCE CLAUSE REQUIRE A CORRELATIVE ADJUSTMENT TO THE NEW MEXICO APPORTIONMENT FACTORS IF SOME PORTION OF THE DIVIDENDS, EXCHANGE GAIN, AND GROSS-UP MAY BE INCLUDED IN APPORTIONABLE BUSINESS INCOME.

A. The Due Process Clause

As discussed above, the basic holding of *Mobil* is that the apportionability of a resident corporation's income to a nondomiciliary State should not be affected by the corporation's choice of corporate structure for conducting its various operations. We pointed out in our main brief that the value of appellant's activities in New Mexico (and the portion of appellant's income properly subject to tax in New Mexico) should not be affected one way or the other by appellant's decision to own foreign businesses as subsidiaries rather than as divisions. We also demonstrated, however, (pp. 33-35) that the amount of appellant's New Mexico taxable income would be disproportionately increased (as a consequence of owning foreign subsidiaries instead of divisions) if the inclusion of the disputed items in apportionable income were not accompanied by a correlative adjustment to the New Mexico apportionment factors.

New Mexico apparently agrees that the amount of appellant's income properly apportioned to New Mexico should not differ depending on the choice of corporate structure. Nor could New Mexico contend otherwise since the value of the intrastate activities in

New Mexico is not affected by the choice of corporate structure. Nevertheless, New Mexico states (N.M. Br. 29):

> Woolworth contends that New Mexico's apportionment statute violates due process because it attributes differing amounts of income to New Mexico, depending merely on the corporate structure of the taxpayer. (Brief of Appellant at 33) The facts do not support this contention.

The fact is, as discussed above, that New Mexico's entire case *is* based on appellant's choice of corporate structure, under which appellant's foreign operations were placed in dividend-paying subsidiaries. New Mexico admits that it could not otherwise have taxed directly the income of those foreign operations; yet it claims to be able to tax dividends paid out of those earnings. Absent correlative factor modification, this approach presents the clearest possible case in which the amount of income apportioned to New Mexico would vary depending on the choice of corporate structure. The result is the same as in the example discussed at pages 33-35 of our main brief, and neither New Mexico nor the MTC has refuted that example.[7]

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[7] The MTC brief (MTC Br. 22) refers to examples on pages 18-22 of its *amicus curiae* brief in *ASARCO Incorporated (formerly the American Smelting and Refining Company)* v. *Idaho State Tax Commission, prob. juris. noted,* —— U.S. ——, No. 80-2015. Those examples are not helpful, since they contain errors and relate to factual situations not present here. For example, the combined reporting calculation on the top of page 20 of the MTC brief in *ASARCO* is erroneous because it includes Corporation B's property, payroll, and sales in the denominators, but not in the numerators, of the apportionment fractions. In any event, the basic issue, which the MTC examples fail to address, is whether the apportionability of income should depend on the choice of corporate structure. New Mexico's position inevitably leads to that result.

In *Mobil*, this Court was confronted with a situation where a single unitary business transcended corporate boundaries and included the activities of the dividend-paying subsidiaries. Here, New Mexico now presses an entirely different ground for including the dividends in apportionable business income—*i.e.*, that the stock of the foreign subsidiaries is an asset of appellant's separate Unitary Business. Apparently, New Mexico believes that because the dividends from this stock are the separate income of appellant, the apportionment fraction can be based solely on appellant's separate payroll, property, and sales. Both New Mexico and the MTC contend that all of appellant's income, including dividends from functionally separate subsidiaries, can properly be apportioned on the basis of a formula which only takes into account factors that relate to appellant's operating income (*i.e.*, appellant's own tangible property, payroll, and sales). See N.M. Br. 31-32; MTC Br. 8-16.

Appellant disagrees. New Mexico's view of the case as involving income from intangibles still would not diminish or alter the need for an adjustment to the New Mexico apportionment factors. Those factors, as presently applied, still fail to account adequately for appellant's substantial investment in major foreign subsidiaries operating totally outside New Mexico. It is true that appellant's out-of-state payroll factor reflects its direct salary costs associated with the oversight of the foreign subsidiaries. But this amount is negligible.[8] The token adjustment that New Mexico

[8] New Mexico chides appellant (N.M. Br. 8-9, 17) for having deducted the payroll expenses associated with oversight of its foreign subsidiaries in arriving at apportionable business income. Conceptually, New Mexico may be correct and appellant would agree to an

has made to the sales factor is also wholly inadequate because the denominator of the sales factor reflects only the dividends, exchange gain, and gross-up in dispute, and *not* the sales of the foreign subsidiaries.[9] Finally, New Mexico has made no adjustment at all to the property factor. Appellant's investments in its large foreign subsidiaries operating entirely outside New Mexico accounted for approximately 76% of appellant's total apportionable income as computed by New Mexico (*viz.*, $66,979,494 out of $87,603,703). (J.A. 57a, 69a) Under these circumstances, a further meaningful adjustment to the apportionment formula is constitutionally required to reflect the out-of-state property, payroll, and sales which produced that income.[10] See the authorities

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appropriate adjustment in this regard on remand. The practical answer, however, is that these expenses were *de minimis*. Cf. *F. W. Woolworth Co.* v. *Commissioner*, 54 T.C. 1233, 1267-1270 (1970) in which the Tax Court held that no expenses of this type need be allocated to Woolworth's foreign source dividend income for federal tax purposes. In any event, appellant's failure to separately account for these minor expenses here affords New Mexico no basis for including almost $67 million of dividends, exchange gain, and gross-up in apportionable income.

[9] The dividends, exchange gain, and gross-up aggregate $66,979,494, whereas appellant's other gross receipts aggregate $2,507,990,364. (J.A. 57a, 69a) Including the disputed items in the denominator of the sales factor only reduced that factor from .528448 of 1%, as reported, to .514233 of 1%. (J.A. 57a, 69a) Equating dividends with gross receipts is indefensible; $1 of dividends (representing *net* profits) should be accorded more weight than $1 of gross receipts (which represents only a few cents of net profits).

[10] Although New Mexico increased appellant's apportionable income from $20,624,209 (the amount originally reported plus an undisputed interest adjustment) to $87,603,703, the apportionment factor was only reduced from .463073 of 1% to .458335 of 1%—hardly an adequate adjustment. (J.A. 57a, 69a)

cited on page 39 of our main brief. The cases cited by New Mexico and the MTC involving intangibles in other contexts simply are not responsive to this problem.[11]

New Mexico also claims repeatedly that appellant has failed to carry its burden of showing that New Mexico's apportionment formula "results in extra-territorial values being taxed." *Butler Bros.* v. *McColgan*, 315 U.S. 501, 507 (1942). For example, New Mexico suggests that $401,518 (the amount of income arrived at under its formula) is not too much to attribute to appellant's retail operations in New Mexico. After increasing apportionable income from $20,624,209 (appellant's agreed operating income) to $87,603,703 (by adding foreign dividends, exchange

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[11] In *Adams Express Co.* v. *Ohio State Auditor*, 165 U.S. 194, *reh'g denied*, 166 U.S. 185 (1897), involving a property tax, the value of the property in Ohio was determined by taking a percentage of the value of the corporation's outstanding capital stock. The intangible assets thus apportioned were the corporation's goodwill and franchises as reflected in the value of the corporation's stock. But these assets are clearly integrated with the underlying business of the corporation and afford no parallel to the issue here—namely, the apportionment of income from investments in separate foreign subsidiaries. This also applies to *Ford Motor Co.* v. *Beauchamp*, 308 U.S. 331 (1939). *Flint* v. *Stone Tracy Co.*, 220 U.S. 107 (1911), involved the imposition of a federal excise tax on corporations and did not address the apportionment issue presented here.

Some of the cited cases involved the situs of intangibles for purposes of property or corporate excise on franchise taxes. To the extent they deal with stock, they hold that the situs is the State of the corporate-stockholder's business headquarters (*First Bank Corp.* v. *Minnesota*, 301 U.S. 234 (1937)) or the domicile of an individual (*First Nat. Bank* v. *Maine*, 284 U.S. 312 (1932). See also *National Leather Co.* v. *Massachusetts*, 277 U.S. 413 (1928).

gain, and gross-up), New Mexico even claims that the resulting attribution of $401,518 to New Mexico may "very well" be the amount of income produced by appellant's local New Mexico activities. (N.M. Br. 28) If so, it would be a remarkable coincidence and irrelevant to the issue presented here.

Appellant submits, as shown by the foregoing discussion, that it has carried its burden. It is not necessary to show that the precise dollar amount arrived at under New Mexico's formula was wrong. *Hans Rees' Sons, Inc.* v. *North Carolina ex rel. Maxwell,* 283 U.S. 123, 136-137 (1931). The issue here is one of methodology—namely, the extent to which New Mexico may constitutionally tax large foreign-source investment income which, as such, did not arise from appellant's local activities in New Mexico. Notice that New Mexico nowhere asserts that appellant's "acquisition, management, and disposition" of its foreign subsidiaries (*i.e.,* the activities which assertedly gave rise to this business income) constituted New Mexico activities; indeed, it concedes just the opposite by (1) describing appellant's New Mexico activities as being limited to the operation of a store, and (2) allocating all of the disputed income items to the denominator (but not the numerator) of the sales factor.

Accordingly, unless the New Mexico apportionment factor is modified, New Mexico's apportionment method will be "inherently arbitrary, or a mere effort to reach profits earned elsewhere under the guise of legitimate taxation." *Bass, Ratcliff & Gretton* v. *State Tax Commission,* 266 U.S. 271, 283 (1924). The dis-

puted income from investments is "in no just sense attributable to transactions within" New Mexico. *Hans Rees' Sons, Inc.* v. *North Carolina ex rel. Maxwell, supra,* 283 U.S. at 134. Consequently, absent factor modification, New Mexico's apportionment method is unconstitutional.

B. The Commerce Clause

Most of New Mexico's Commerce Clause arguments have been dealt with in our main brief. There are several points, however, that warrant a further response here.

First, New Mexico questions whether our Foreign Commerce Clause argument was adequately raised below. In particular, New Mexico states (N.M. Br. 42):

> The argument that Woolworth's dividends should not be allocated to the state of commercial domicile has not been presented to any New Mexico court or administrative body. The Supreme Court's review is limited to the specific federal question that was raised in the courts below. *See Wilson* v. *Cook,* 327 U.S. 474, 483 (1946). Woolworth cannot now maintain that its change in position is insignificant and the Court should decline to review this point.

As is set forth in detail in our main brief, our Foreign Commerce Clause argument is based on New Mexico's failure to adjust the apportionment factors, thereby permitting New Mexico to impose a direct tax on foreign-source investment income that has already been taxed abroad. Furthermore, since the laws and treaties of this Nation explicitly provide (in accord-

ance with international custom) for the avoidance of such double taxation at the federal level, New Mexico's failure to use some mechanism that will avoid international double taxation at the state level prevents this Nation from speaking with one voice in matters that affect this Nation. Appellant's brief in the New Mexico Supreme Court contains precisely the same argument as follows (pp. 29-30):

> . . . failure to provide a foreign tax credit or eliminate the double tax effect will result in the *international double taxation* that violates the Foreign Commerce Clause. *Japan Line, Ltd.* v. *County of Los Angeles,* 441 U.S. 434 (1979). (Emphasis supplied.)

Our assertion that the foreign-source investment income may not be taxed by either a State of commercial domicile or a nondomiciliary State is merely a refinement of this basic Foreign Commerce Clause argument, and is properly presented here. Cf. *Commissioner* v. *Gordon,* 391 U.S. 83, 95, n.8 (1968). For, as this Court pointed out in *Mobil,* 445 U.S. at 447, if the State of commercial domicile may tax the income, then the issue is not one of international double taxation but of duplicative state taxation, a problem that can be avoided through proper apportionment. In view of this portion of the Court's decision in *Mobil,* which was announced following the submission of appellant's brief to the New Mexico Supreme Court,[12] it is appropriate for appellant to clarify its position in this Court as to the right of the State of

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[12] *Mobil* was decided on March 19, 1980. Appellant's brief in the New Mexico Supreme Court was filed on March 11, 1980. (J.A. 3a)

commercial domicile to tax the dividends in issue.[13] Finally, the same legal question is before the Court in *ASARCO Incorporated (formerly the American Smelting and Refining Company)* v. *Idaho State Tax Commission, prob. juris. noted,* —— U.S. ——, No. 80-2015. Under these circumstances, appellant's Commerce Clause argument is properly before the Court.

New Mexico also contends (N.M. Br. 42) that "the record does not indicate what taxes were paid on Woolworth's dividends abroad." As we showed in our main brief (pp. 43-44), Australia, Germany, Mexico, and the United Kingdom all imposed an income withholding tax on the full amount of dividends in issue. Technically, as this Court has held, a state tax violates the Commerce Clause if it merely "creates a substantial *risk* of international multiple taxation." *Japan Line, Ltd.* v. *County of Los Angeles,* 441 U.S. 434, 451 (1979) (emphasis supplied). In this case, it is undisputed that appellant was subject to tax on its dividend income in all four foreign countries involved, with the result that appellant's foreign-source dividends would clearly be subject to multiple international taxation if New Mexico's position were upheld. Accordingly, under these circumstances, it is unnecessary to demonstrate that the foreign tax liabilities were, in fact, paid.

The key issue here is whether, as appellant claims, New Mexico has taxed directly, by its failure to adjust its apportionment factors, a portion of appellant's

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[13] This Court also has held that when a new argument is made in response to an intervening court decision, the argument may be considered. *Hormel* v. *Helvering,* 312 U.S. 552, 557-559 (1941). The refinement of our general Foreign Commerce Clause argument in this case does not even go that far.

foreign-source investment income which was earned outside New Mexico. If appellant's view is correct, then New Mexico's inclusion of the disputed items in income without an adequate adjustment to the apportionment factors inevitably results in multiple foreign and state taxation. New Mexico inferentially recognizes that the Foreign Commerce Clause is applicable if "New Mexico has overreached and taxed income which is attributable to foreign activities." (N.M. Br. 44) But New Mexico asserts (N.M. Br. 45) that "the dividend income in question is attributable to Woolworth's activities in the United States."

There simply is no support for New Mexico's view. The dividends are "foreign-source," earned by investments made outside of New Mexico in foreign subsidiaries operating outside New Mexico. The income cannot be said to be directly attributable to any activities in New Mexico.[14] New Mexico cites Hellerstein, *State Income Taxation of Multijurisdictional Corporations: Reflections on Mobil, Exxon and H.R. 5076,* 79 Mich. L.Rev. 113, 166 (1980), as support for its position. In fact, Professor Hellerstein's article directly supports our position here. Professor Hellerstein does say (pp. 168-169) that a State may include foreign-source dividends in taxable income, *but only where the inclusion of such dividends is accompanied by an appropriate adjustment to the apportionment factors.* Similarly, in his discussion of this Court's decision in *Mobil,* Professor Hellerstein states (pp. 127-128):

> But the Court's remarks were directed to cases in which the factors—real and tangible personal

[14] See also pp. 14-15, *supra.*

> property, payroll and sales—were rationally related to the operating income of the taxable corporation. By contrast, Vermont was applying its formula to income that, in form at least, derived from Mobil's investments in its subsidiaries and affiliates, not from its operations. When a corporation receives between 80 and 120% of its taxable income from intangible property, it is anomalous—and perhaps grossly distorting—to apportion such income by a formula that, among other things, takes no account of intangible property. (Footnotes omitted.)

Professor Hellerstein's article rejects the result which New Mexico seeks to defend here. There is no support for the inclusion of such substantial foreign-source dividends in the apportionable income base without a correlative adjustment to the apportionment factors.

Finally, as to New Mexico's argument concerning the applicability of *Japan Line, Ltd.* v. *County of Los Angeles, supra,* to income tax cases, we note that our position in that regard is fully supported by the *Amicus Curiae* Memorandum of the United States in *Chicago Bridge & Iron Company* v. *Caterpillar Tractor Co., Illinois Department of Revenue et al., prob. juris. noted,* —— U.S. ——, No. 81-349. Furthermore, the United States also supports our view that the decision in *Mobil* did not consider our Foreign Commerce Clause argument in view of the concession in *Mobil* that the dividends there in issue could be taxed by the State of commercial domicile. See the footnote on page 16 of the United States' Memorandum.

CONCLUSION

For the foregoing reasons and for the reasons stated in appellant's main brief, this Court should reverse the decision below and remand the case to the Supreme Court of New Mexico for further proceedings.

Respectfully submitted,

GEORGE W. BEATTY
(Counsel of Record)
WILLIAM L. GOLDMAN
JAMES A. RIEDY
1200 18th Street, N.W.
Washington, D.C. 20036
(202) 457-8528

MICHAEL D. BRAY
30 Rockefeller Plaza
New York, N.Y. 10112

Counsel for Appellant

ARNOLD S. ANDERSON
ALAN J. LIPNER
233 Broadway
New York, N.Y. 10279

Of Counsel

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